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IN THE

Supreme Court of the United States

OCTOBER TERM, 1967

NO. ~~1391~~ 161

In the Matter of: LENRICK SALES, INC., Bankrupt,
Appellant

v.

JAMES TALCOTT INC., SHAPIRO BROS. FACTORS CORP., CROMPTON-RICHMOND CO., INC., Appellee

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT, AND APPENDIX.

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In the Matter of: LENRICK SALES, INC., Bankrupt,
AARON COHEN, Trustee,
Appellant

v.

JAMES TALCOTT INC., SHAPIRO BROS. FACTORS CORP. AND CROMPTON-RICHMOND CO., INC.

(D. C. NO. 66-16 IN BANKRUPTCY)

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

To The Honorable, The Chief Justice and The Associate Judges of The Supreme Court of the United States:

Your petitioner, Aaron Cohen, Trustee of the Estate of Lenrick Sales, Inc., bankrupt, prays that a Writ of Certiorari be issued to review the judgment of the Court of Appeals for the Third Circuit entered on February 15, 1967, reversing the judgment of the United States District Court for the Western District of Pennsylvania, filed May 17, 1966, and remanding the cause to the District Court for entry of an Order directing the Referee to vacate the Trustee's appointment and to promptly give notice of a new meeting of creditors to elect a Trustee.

OPINIONS OF THE COURT BELOW.

The opinion of the Court of Appeals, as well as the opinion of the District Court does not appear in the official and unofficial reports of the opinions delivered in the respective courts.

The opinion of the Court of Appeals is set forth in the appendix attached hereto.

The opinion of the District Court is set forth in the Appendix attached hereto.

JURISDICTION.

The judgment of the Court of Appeals was entered on February 15, 1967.

The jurisdiction of your Honorable Court is invoked under Title 11 U.S.C. Sec. 47 (c).

QUESTIONS PRESENTED.

1. Did the learned Court of Appeals err in approving, in effect, claim of illegality and inappropriate procedure, by the Referee in Bankruptcy, in filing findings and conclusions *after* he had the petition for review in hand contrary to the decision of the Court of Appeals of the 6th Circuit (*In re: DIA Sales Corporation et al.* 339 Fed. (2) 175 at page 180 (1964)) holding that the certificate of the Referee upon review contained adequate findings of fact and conclusions of law and that it was not necessary for him to have set forth these same findings and conclusions in the order?

Questions Presented.

2. Did the learned Court of Appeals err in failing to give effect to specific findings of fact by the Referee in the certificate of the Referee that one of the nominees for the trustee was unacceptable because of "prejudicial association" with interest adverse to that of all the creditors, coupled with the exercise of proxies never intended to be voted in the bankruptcy proceeding, causing delay and loss to the estate, in the exercise of the Referee's discretion, in the broad sense, including the personal judgment of the Referee supported and approved by the District Court, in the absence of finding by the appellate court of a demonstration of plain mistake and contrary to the interpretation and decisions of other courts of appeal, (6th Circuit and 9th Circuit) *Re: DIA Sales Corporation* (6 CCA) 339 Fed. (2) 175; *Lyons v. Falstaff Brewing Co.* 233 Fed. (2) 927, page 932-933-934 (9 C.C.A.).

3. Did the learned Court of Appeals err in failing to recognize the mandate of the provision of the Bankruptcy Act (Sec. 44 (a) 11 U.S.C. Sec. 72, to the effect that "the creditors of a bankrupt . . . *shall* at the first meeting of creditors after adjudication . . . appoint a trustee or three trustees of such estate—if the creditors do not appoint a trustee . . . the court *shall* make the appointment", which provision of the Bankruptcy Act has not but should be settled by the Supreme Court"?

4. Did the learned Court of Appeals err in entertaining an appeal in the absence of a record of testimony in the proceedings before the Referee in Bankruptcy, due to the unavailability of court funds, and, the appellant's failure to invoke the substitute proceedure under the Bankruptcy Act (Sec. 39 (a) (7) 11 U.S.C. Sec. 67

and the Rules of Civil Procedure (Sec. 75 (c)) and in the absence of the only permissible method of challenging the exercise by the Referee of an administrative act in appointment of a Trustee, directly, by motion to vacate the appointment in conflict with the decision of the Court of Appeals of the 8th Circuit as expressed in *Kimm v. Cox,* 130 Fed. (2) 721, 736?

5. Did the learned Court of Appeals err in failing to apply the Rule 52 (a) of the Federal Rules of Civil Procedure in the instant case where the trustee had been appointed and assets of the business had been sold at that time and no good purpose could be accomplished by reversal almost eleven months later, of the appointment of the Trustee, in conflict with the decision of another court of Appeals, to-wit: Ninth Circuit. In *Manhattan Shirt Co. v. Tomlinson, Trustee,* 327 Fed. (2) 449 (1964) and Federal Rules of Civil Procedure 61?

6. Did the learned Court of Appeals err in finding justification of delay and increase in administrative expense contrary to the finding of the Referee and the District Court on the ground of violation of creditors' right to appoint under circumstances of disagreement on a choice of credit rs, indefinite delay for determination of objections to allowance on part of other creditors, excusable from the challenged premise that appellants and those associated with them represented more than 95% in amount of the unsecured creditors, without due regard to the rights of all the creditors contrary to decision of other courts of appeal? *In Re-McGill* CCCA 6th Cir.) (1901) 106 Fed. 57 5 ABR 155, *Schwartz v. Mills* (CCA2) 192 Fed. (2) 727,728.

STATUTORY PROVISIONS INVOLVED

1. 11 U.S.C. Sec. 1 under the Bankruptcy Act, Sec. 1 (9) "Court shall mean the judge or the Referee of the Court in Bankruptcy in which proceedings are pending."

2. 11 U.S.C. Sec. 11 under the Bankrupt Act, Sec. 2 (17) "Approve the appointment of trustees by creditors or appoint trustees when creditors fail so to do; and upon complaints of creditors and upon their (Referee's own motion, remove for cause receivers or trustees upon hearing after notice."

3. 11 U.S.C. Sec. 92 Bankruptcy Act, Sec. 56. "Voters at Meetings of Creditors. A Creditor shall pass upon matters submitted to them at their meetings by a majority vote in number and amount of Claims of all creditors whose claims have been allowed and who are present, except as herein otherwise provided."

4. 11 U.S.C. Sec. 67 (a) (7) Bankruptcy Act, Sec. 39, sub-paragraph (a) (7); "Upon application of any party in interest, preserve the evidence taken, or the substance thereof as agreed upon by the parties before them when a stenographer is not in attendance."

5. 11 U.S.C. Sec 67, under the Bankruptcy Act, Sec. 39 sub-paragraph 8: "Prepare promptly and transmit to the clerks certificates on petition for review of orders made by them, together with a statement of the questions presented, the findings and orders thereon, the petition for review, a transcript of the evidence, or, a summary thereof, and all exhibits."

6. 11 U.S.C. Sec. 72 under the Bankruptcy Act, Sec. 44 (a): "The creditors of bankrupt, exclusive of

the bankrupt's relatives, or, where the bankrupt is a corporation, exclusive of its stockholders or members, its officers, and the members of its board of directors or trustees, or, of other similarly controlling bodies, ***shall,*** at the first meeting of creditors after the adjudication, or after the vacancy has occurred in the office of the trustee, or after an estate has been re-opened, appoint a trustee or three trustees of such estate. If the creditors do not appoint a trustee, or, if the trustee so appointed fails to qualify as herein provided, the court ***shall*** make the appointment . . ."

GENERAL ORDERS INVOLVED

General Orders in bankruptcy adopted by the Supreme Court of the United States as amended May 29, 1961, effective July 19, 1961.

37. "In proceedings under the Act, the Rules of Civil Procedure for the District Courts of the United States shall, insofar as they are not inconsistent with the Act or with these general orders, be followed as nearly as may be."

47. *"Reports of Referees and special masters.* Unless otherwise directed, in the order of reference, the report of a referee or of a special master shall set forth his findings of fact and conclusions of law, and the judge shall accept his findings of fact unless clearly erroneous. The judge after hearing may adopt the report or may modify it or may reject it in whole or in part, or may receive further evidence or may recommit it with instructions.

FEDERAL RULES OF CIVIL PROCEDURE INVOLVED

1. Rule 52 (a): "Effect. In all actions tried upon the facts without a jury, or with an advisory jury, the court shall find the facts specially and state separately its conclusions of law thereon and direct the entry of the appropriate judgment; and in granting or refusing interlocutory injunctions, the court shall generally set forth the findings of fact and conclusions of law which constitute the grounds of its action. Request for findings are not necessary for the purpose of review. Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opinion of the trail court to judge of the credibility of the witnesses. The findings of a master, to the extent that the court adopts them, shall be considered as the findings of the court. If an opinion or memorandum of decision is filed, it will be sufficient if the findings of fact and conclusions of law appear therein. Findings of fact and conclusions of law are unnecessary on decisions of motions under Rule 12 or 56 or any other motion except as provided for in Rule 41 (b)."

2. Rule 61 General Rules of Civil Procedure for the United States District Court: "Harmless error. No error in either the admission or the exclusions or evidence and no error or defect in any ruling or order or in anything done or omitted by the Court or by any of the parties is ground for granting a new trial, or, for setting aside a verdict, or for vacating, modifying, or otherwise distrubing judgment or order, unless refusal to take such action appears to the court inconsistent with substantial justice. The court at each stage of the

proceedings must dismiss any error or defect in the proceeding which does not affect the substantial rights of the parties."

3. Rule 75 (c): "Statement of the evidence or proceedings when no report was made, or when the transcript is unavailable, if no report of the evidence or proceedings at a hearing or trial was made, or if a transcript is unavailable, the appellant may prepare a statement of the evidence or proceedings from the best available means, including his recollection. The statement shall be served on the appellee, who may serve objections or propose amendments thereto within ten days after service. Thereupon the statement and any objections or proposed amendments shall be submitted to the District Court for settlement and approval and if settled and approved shall be included by the clerk of the District Court in the record on the appeal."

STATEMENT OF THE CASE

The case involves a review of the order of the Honorable Joseph P. Willson, Judge of the United States District Court for the Western District of Pennsylvania, in all respects adopting the report of Stephen P. Laffey, the Referee in Bankruptcy, which included a brief history of the proceedings originating with the filing of a petition for an arrangement under Sec. 322 of Chapter XI of the Bankruptcy Act with the debtor authorized to remain in possession; and extension of time for filing of schedules and filing of plan of arrangement and subsequent withdrawal of the petition for an arrangement, request for adjudication of the bankrupt, and, appointment of Aaron Cohen, Esq., as the receiver.

The petition for review alleged the petitioners, briefly three creditors, who were factors of the debtor were aggrieved by reason of an Order made by the Referee in Bankruptcy under date of March 21, 1966 reciting that, the creditors having failed to appoint a trustee, at the first meeing of creditors, pursuant to regulation to bankruptcy, that he, the Referee, had appointed Aaron Cohen to be the trustee; the petition for review prayed that the Referee's Order be vacated and that an Order be entered *approving the appointment* of one, Norton L. Berman, as trustee.

The petition for review did not ask for a re-election of trustee, but was confined solely to the request to vacate the appointment of Aaron Cohen as appointed by the Referee, and, in his stead, that the Judge of the District Court make the appointment of one, Norton L. Berman, as trustee.

The petition for review had alleged that Norton L. Berman as trustee had been elected by majority in number and amount of claims of all creditors present in person, or, by proxy.

The petition for review averred that the Referee "on his own objection", refused to accept the results of the election on the grounds that Aaron Cohen previously had been appointed Receiver and that there had been "innuendos" that some of the claims which had voted for Berman had been solicited.

The main gravamen of the petition for review related to the refusal of the Referee to authorize appointment of a creditors' committee.

Upon appeal, from dismissal of the petition for review, to the Court of Appeals for the Third Circuit, the argument of the appellants revolved around the claim that the claims represented by informal creditors' committee had been refused opportunity to vote at an election of the trustee, an obvious patent contradiction between the petition for review of the Referee's Order of appointment of the Trustee and the subsequent grounds for vacation urged before the Court of Appeals. The petitioner attaches a copy of the Petition for Review as part of the appendix attached and annexed hereto, following the opinion of the Circuit Court of Appeals.

(Appendix Page 21)

The first meeting of creditors was held before Stephen P. Laffey, Referee in Bankruptcy on March 21, 1966, at which a representative of the committee armed with 65 proofs of claim and proxies previously obtained in connection with the prior Chapter XII Proceeding, indicated his intention to vote these claims for one, Norton L. Berman. The representative of those creditors

whose claims had been previously filed and allowed had indicated their intention to vote for Aaron Cohen, Esq., who had served as the Receiver in a practically liquidated estate. None of the creditors were present in person. All 65 proxies not filed prior to the creditors' first meeting were challenged and remained for adjudication after full hearing.

A stenographic record of the proceedings before the Referee was not taken, due to the admitted circumstances that in the Western District of Pennsylvania, parties are free to arrange to have a reporter present at their own expense, but the Court does not have funds to employ a reporter for the Referee.

The representative of the informal creditors' committee having in his possession the 65 claims, did not actually file his claims until subsequent to the close of the meeting.

The discussion and charges made at the meeting before the Referee were not taken by a reporter, so that no stenographic record was made of the proceedings. The attorneys representing creditors, including that of the representative of the informal creditors' committee were aware of a long standing practice in the Western District of Pennsylvania to the effect that those requiring a stenographic record of the proceedings to be made, must furnish a competent reporter at their own expense, for the reason that the Court does not have the funds to employ, and, does not as a matter of course, employ a reporter for the Referee.

No application by any party in interest was made to preserve the evidence taken or the substance thereof as agreed upon by the parties before them, when a

stenographer is not in attendance, pursuant to 11 U.S.C. 67, objections having been voiced to the proposal for voting of those claims in the apparent control of representative of the informal creditors' committee, organized during the pendency of the arrangement proceeding, by reason of improper solicitation, and unauthorized exercise of proxies obtained for the purpose of the arrangement.

The Referee expressed a willingness to hold a hearing on the following day, which offer was declined by the representative of the informal creditors' committee.

The Referee after examination of the bankrupt considering that the claims previously filed and allowed, by their representatives then present, having nominated Aaron Cohen, *being in disagreement with the representative of an informal creditors committee having nominated Norton L. Berman,* did assume to exercise the right of appointment of trustee, and expressed his choice in favor of the former Receiver, Aaron Cohen, to continue to administer and close the bankrupt's estate as Trustee, and entered an Order to this effect under date of March 21, 1966, at the time of the first meeting of creditors.

No written objection was entered by creditors at said meeting against the appointment of Aaron Cohen.

No motion to vacate the appointment of Aaron Cohen as trustee was made to the Referee. No written application was made by representative of an informal creditors' committee for a hearing date on the claims subsequently filed by representatives then present for the informal creditors' committee, and, no objection was entered to the matter pending before the Referee au-

thorizing the Receiver to consummate proofs of adjusted fire loss.

On March 31, 1966, a local attorney representing three of the creditors, whose representatives served on an informal creditors' committee, during the aborted Chapter XI proceeding, filed petition for review of the Referee's Order seeking reversal and vacation of the Order of the Referee of March 21, 1966 appointing Aaron Cohen as Trustee, and the entry of an Order appproving Norton L. Berman as Trustee and that a meeting of creditors be called for the purpose of appointing a creditors' committee.

There is no request in this petition that upon vacation of the appointment of Aaron Cohen as Trustee that a new election be held, and, on the basis of this petition for review, Judge Willson of the District Court *after full argument, and, after the filing of briefs by counsel for the petitioner and counsel for the Trustee, Aaron Cohen,* filed his opinion on May 17, 1966, dismissing the petition for review and adopting the report of the Referee in Bankruptcy in all respects.

The petitioners for review then filed an appeal with the Circuit Court of Appeals for the Third Circuit, which after argument and consideration of briefs filed by appellants and by Aaron Cohen, Trustee, filed an opinion on February 15, 1967, reversing the judgment of the District Court and remanding the matter to the District Court for an Order directing the Referee to vacate the Trustee's appointment, and the noticing of a new meeting of creditors to elect a trustee.

ARGUMENT

The underlying issue in this petition for writ of certiorari is the degree of authority vested in a court of bankruptcy to control the selection of a trustee in a bankruptcy case upon disagreement of the creditors.

This degree of authority has not been precisely settled by any decisions, directly, by the Supreme Court, and, has given rise to some disparity on the part of the courts of appeal in different circuits.

The decision of the Court of Appeals for the Third Circuit arises from its willingness to accept an appeal from the order of the District Court of Western Pennsylvania pursuant to petition for review which sought appointment of a Trustee by the District Court of a rival nominee for Trustee rather than a vacation of the Referee's appointment and remand for a new election at a second "first meeting of creditors."

The learned Appeals Court took notice of the lack of an official reporter of proceedings before the Referee, due to lack of available court funds, in contrast to such availability in other jurisdictions.

Incidental thereto, the Appeals Court criticized the Referee's failure to set forth findings and conclusion antecedent to entry of his order of appointment of a Trustee at the first meeting of creditors and until after the filing of the petition for review. In the Sixth Circuit the Court of Appeals in *DIA Sales v. Irwin Ray Wm. C. MacGuire Trustee* 339 Fed (2) 180; it was held "We find no merit in appellants' contention that the order of the Referee was defective in that it failed to set forth his findings of fact and conclusions of law. In the footnote we have quoted from the finding of fact and conclusions and that it was not necessary for him to set

forth these same findings and conclusions in the order." See also *Berman & Co.* (CCA 6) 343 Fed. (2) 125, 126.

The Court of Appeals in the case at bar rejected at least in part the substance of findings in the memorandum opinion of the Referee as post hearing. In the absence of a stenographic report of the hearing and meeting of creditors, this limitation placed a narrow limitation on the scope of a Referee's "report" under General Order #47 to the District Court pursuant to petition for review, on the differentiation in scope of "report" of a strictly judicial determination as compared to exercise of an administrative function, in the choice of a Trustee.

In re: *Dalsimer* D. C. N. Y. S. D. 56 Fed (2) 644, it was held "The Court cannot shut its eyes to what is general knowledge or to what it has ascertained by "adequate inquiry."

A narrow limitation to the report of the Referee for the information of the District Court would, of necessity, exclude the personal judgment and findings of the Referee on what has been the most frequent basis for disapproval of the creditors choice, to-wit: "prejudicial association" with interests adverse to those of the estate or *in favor of a special group of creditors.* 14 Ed. Colliers Vol. 2, page 1651 *In Re*: *Kal W. Lyons appellant v. Falstaff Brewing Co.* (9 C.C.A.) 223 Fed (2) 927 which holds "in the appointment of a trustee in bankruptcy mere honesty of the candidate is not enough. The influences back of his appointment are also important" and approval of what was said in re: *Delno v. Market St. Railway Co.* (9 CCA). 124 Fed (2), 965, 967, in defining "area of discretion" (page 932) "In a second

sense and the one most commonly meant in the use of the word in the law, "discretion" is defined as "The power exercised by courts to determine questions to which no strict rule of law is applicable, but which, from their nature and the circumstances of the case, are controlled by the personal judgment of the court. 1 Bouv. Law Dict. Bowles Third Revision page 884."

Sec. 44 (a) of the Bankruptcy Act (11 U.S.C. #72) directs that creditors of a bankrupt *shall* at the first meeting of creditors appoint a trustee. If the creditors do not appoint, the court *shall* make the appointment.

Noteworthy is the absence of any *qualification* to the mandate to act at the first meeting of creditors. Congress no doubt intended that the administrative function of selection of a trustee should be prompt. *Colliers,* 14 Ed. Vol. 2 page 1647 teaches "If possible, there should be no postponement of the election of trustee. *In re*: *Henschel* (CCA 2) 113 Fed. 443 *In re*: *Scully* (D. C. Pa.) 108 Fed. 372. *Abraham v. Shinberg* (CA.D.C.) 190 Fed. (2) 595. While there have been deviations from the statutory directive, the permissible deviation has not been settled by the Supreme Court and, should be, in the interest of the desired expedition of administration.

The pendancy of the case before the Referee for a period from January 10, 1966 until date of first meeting on March 21, 1966 during the practical liquidation of the bankrupt's estate and sudden appearance of some 65 unfiled claims by a representative, for allowance to vote at election of a trustee, the absence of stenographic report, exposed the risk of delay, and added expense, by unusual pressure upon the Referee, against strict compliance with the requirements of the statute.

The decision of the Court of Appeals, drew inferences, in the absence of testimony, solely from findings and conclusions of the Referee, and adoption by the District Court, in contra distinction, to the broad scope of allowable discretion given to the Referee and the supervisory control of the District Court Judge as taught in *Kal Lines v. Falstaff Brewing* (CCA 9) 233 Fed (2) 927; *Manhattan Shirt case* (CCA 9) 327 Fed (2) 449; *Sloan Furrier v. Bradley* (CCA 6) 146 Fed (2) 757; *Garrison v. Pillord* 50 Fed (2) 1035 (10 CCA) and *Leader Mercantile v. Graham Brown Shoe Co.* 36 Fed (2) 745; *Delno Market Street Railway Co.* (9 CCA) 124 Fed (2) 965, which called for judicial restrain in preserving the broad exercise of discretion vested in the Referee and District Court as a Court of Bankruptcy, for the prompt and effective administration of bankrupt's estate, in due regard to the exportise of the Referee in Bankruptcy, in purely administrative matters, as the selection of a Trustee, absent any evidence of plain mistake; *In re Euclid* (CCA 6) 104 Fed (2) 712, *J. B. Cianchelli & Son* 362 Fed (2) 500; *Smith v. Robinson* 343 Fed (2) 793; *Re Berman & Co.* 343 Fed (2) 125; *DIA Sales Corp* 339 Fed (2) 175; *Olympic Finance Co. v. Thyret* 337 Fed (2) 62 certiorari denied; *W. J. Earhart v. Alfred J. Callan, Jr.* 221 Fed (2) 160 certiorari denied.

The reversal of the District Court, in the circumstance that the estate, perishable in nature, had been practically liquidated, and nothing remained but for the Trustee to make distribution, is incompatible with the intent and purpose of Rule 61, Federal Rules of Civil Procedure and results in an "utterly futile procedure." *Sloan Furriers v. Bradley,* 146 Fed (2) 757; *Manhattan*

Shirt Co. 327 Fed (2) 449; *Karl W. Lines v. Falstaff Brewing Co.* (9CCA) 233, Fed (2) 928 and *Delno v. Market Street Railway Co.* (9CCA) 124 Fed (2) 965.

CONCLUSION

The ultimate decision of the Court of appeals that the District Court committed error in basing the dismissal of the petition for review on the ground that "creditors failed to appoint a Trustee" failed to take account of Referee's finding that "Aaron Cohen was duly nominated and elected by the majority in number and amount of the valid claims filed and allowed", and absence of any record to the contrary or any petition to vacate his appointment was conclusive whether the appointment was recited to have been made by election or Referee's subsequent appointment which in effect served to ratify, approve and confirm the election by the exercise of valid claims filed and allowed, in the face of the undetermined status of contested claims and all the circumstances of the case, avoiding delay and expense, and affording protection of the interest of all creditors, as opposed to the undefined suspect interest of a few disgruntled representatives of creditors whose proxies were in the process of being contested. *Matter of Knox* (CCA6) 221 Fed. 36; *In re Clay* (CCA1st) 192 Fed. 830.

For the foregoing reasons it is respectfully submitted that the Court should grant Writ of Certiorari.

Respectfully submitted,

HARRY R. LEVY
AARON COHEN,
Attorneys for Petitioner.

APPENDIX

UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

IN THE MATTER OF LENRICK SALES INC., a Pennsylvania corporation Bankrupt	In Bankruptcy No. 66-16

Appointment of Trustee by Referee

At Pittsburgh, Pa., in this district, on the 21st day of March, 1966.

[*If the creditors elect a trustee, use paragraph (1) and strike paragraph (2); if the creditors fail to elect a trustee, use paragraph (2) and strike paragraph (1).*]

(2) The creditors of the above-named bankrupt having failed to appoint a trustee as provided in the Bankruptcy Act, Aaron Cohen, of Pittsburgh, Pa., is hereby appointed trustee of the estate of the bankrupt, and the amount of his bond is fixed at Fifteen Thousand ($15,000.00) dollars.

STEPHEN P. LAFFEY
Referee in Bankruptcy.

Petition for Review

To the Honorable Stephen P. Laffey, Referee in Bankruptcy:

The petition of James Talcott, Inc., Shapiro Bros. Factors Corp. and Crompton-Richmond Co., Inc. Factors respectfully alleges:

1. Petitioners are aggrieved by reason of the order made by Honorable Stephen P. Laffey, Referee in Bankruptcy (dated March 21, 1966 approving the appointment of Aaron Cohen as Trustee in Bankruptcy. A copy of said order is hereto annexed, marked Exhibit "A" and made a part hereof.

2. Petitioner James Talcott, Inc. is a general unsecured creditor of the bankrupt herein for the sum of $19,261.16. Petitioner Shapiro Bros. Factors Corp. is a general unsecured creditor of the bankrupt herein for the sum of $14,393.95. Petitioner Crompton-Richmond Co. Inc. Factors is a general unsecured creditor of the bankrupt herein for the sum of $10,471.30.

3. On January 10, 1966 the above-named Lenrick Sales, Inc. filed an original petition for an arrangement under Section 322 of the Act of Congress relating to Bankruptcy. No meeting of creditors was called as required by Section 334 of said Bankruptcy Act. Thereafter, Lenrick Sales Inc. as debtor in said arrangement proceeding petitioned the Court to be adjudicated a bankrupt. An order was entered adjudicating it a bankrupt, directing that bankruptcy be proceeded with and appointing Aaron Cohen as Receiver.

4. In accordance with the provisions of the Bankruptcy Act, the Honorable Stephen P. Laffey, Referee in Bankruptcy caused a first meeting of creditors of Lenrick Sales Inc., bankrupt, to be held before him on March 21, 1966 at Room 9, United States Courthouse, in the City of Pittsburgh, State of Pennsylvania. Notice was given to creditors to attend such meeting and that at such meeting they might "appoint a trustee, examine the bankrupt and transact such other business as may properly come before said meeting."

5. On March 21, 1966 at the aforesaid meeting of creditors in the bankruptcy proceeding, one of the matters proceeded with was for the appointment of a trustee. Norton L. Berman and Aaron Cohen were nominated. 61 unsecured creditors had executed proxies to an unsecured Creditors' Committee consisting of Joseph A. Zeller, David Horner, Nathaniel P. McCaffrey, Seymour Benson and Milton Gittenstein, by any member thereon and/or their representatives. David Horner as a member of such Creditors' Committee appeared and voted said 61 claims for Norton L. Berman as Trustee. George A. Hahn, Esq. with proxies from four (4) more unsecured creditors of the bankrupt voted the claims of such four (4) creditors for Norton L. Berman as Trustee. A total of 65 unsecured claims aggregating $113,738.99 were voted in favor of Norton L. Berman as Trustee. Not a single claim was voted for Aaron Cohen. However, the Referee on his own objection, refused to accept the results of the election upon the grounds that Aaron Cohen previously had been appointed Receiver and that there had been "innuendos" that some of the claims which were voted for Norton L.

Berman had been solicited. The 65 aforementioned creditors through their representatives also sought to nominate a Creditors' Committee but the Referee refused to allow the nomination of a Creditors Committee, stating that he did not see any necessity for appointing one.

6. The Referee erred when, contrary to and in derogation of the provisions of the Bankruptcy Act, he arbitrarily arrogated to himself entirely the choice of a Trustee and refused to appoint Norton L. Berman as Trustee despite the latter's election by a majority in number and amount of the claims of all creditors present in person or by proxy at such meeting. The pertinent provisions of the Bankruptcy Act are as follows:

> § 44a: "The creditors of a bankrupt . . . shall, at the first meeting of creditors after the adjudication . . . appoint a trustee or three trustees of such estate . . ."
>
> § 56a: "Creditors shall pass upon matters submitted to them at their meetings by a majority vote in number and amount of claims of all creditors whose claims have been allowed and who are present, except as herein otherwise provided."

7. The Referee erred in finding that Aaron Cohen's prior appointment as Receiver gave such person some special claim to be Trustee which could override the results of the election at the first meeting of creditors.

8. The Referee erred in accepting "innuendos" and hearsay about solicitation as substitution for a hearing thereon with testimony and other proof.

9. The Referee erred in holding that claims solicited by the aforementioned Creditors' Committee should be disregarded. Creditors or a Creditors' Committee have the absolute right to solicit claims of other creditors for the purpose of voting such proxies for the appointment of a Trustee so long as the purpose thereof is not in the interests of the bankrupt.

10. The Referee erred in refusing to allow nominations for a Creditors' Committee. Such action was a usurpation of the rights of creditors, a flouting of the provisions of the Bankruptcy Act and a decision of the most extreme arbitrariness. Section 44b of the Bankruptcy Act provides:

> "Such creditors may, at their first meeting, also appoint a committee of not less than three creditors, which committee may consult and advise with the trustee in connection with the administration of the state, make recommendations to the trustee in the performance of his duties and submit to the court any question affecting the administration of the estate . . ."

WHEREFORE, your petitioners pray that the order of March 21, 1966 appointing Aaron Cohen Trustee be reviewed by a Judge in accordance with the provisions of the Act of Congress relating to Bankruptcy, the said order be reversed and vacated, that an order be entered approving the appointment of Norton L. Berman as Trustee, that a meeting of creditors be called for the purpose of appointing a Creditors' Committee as pro-

vided in the Bankruptcy Act, and that your petitioners have such other and further relief as is just.

Dated: New York, New York,
March 29, 1966.

JAMES TALCOTT, INC.,
By: JOSEPH GUARASCIO,

SHAPIRO BROS. FACTORS CORP.,
By: SIDNEY B. GLUCK,

CROMPTON-RICHMOND CO. INC. FACTORS,
By: NATHANIEL P. MCCAFFREY,

BERGER & BERGER,
Attorneys for Petitioners,
By:
Member of Firm,
508 Law & Finance Building,
Pittsburgh, Pennsylvania 15219,

HAHN, HESSEN, MARGOLIS & RYAN,
Attorneys for Petitioners,
By: GEORGE A. HAHN,
Member of Firm,
350 Fifth Avenue,
New York, New York 10001.

(Affidavits omitted.)

Referee's Certificate of Order for Review

I, STEPHEN P. LAFFEY, one of the Referee's of said Court in Bankruptcy, do hereby certify that in the course of the proceedings in said cause before me, the following question arose pertinent to said proceeding.

Should the person nominated as Trustee and receiving votes by the majority in number and amount of the creditors be elected Trustee?

I answered this question in the negative.

Petitioners deeming themselves aggrieved thereby, and through their counsel, filed a Petition for Review on March 31, 1966.

Herewith transmit are:

1—Referee's Memorandum Opinion, Findings of Fact and Conclusions of Law, filed April 14, 1966.

2—Petition for Review filed March 31, 1966.

And the said Order is certified to the Judge for his decision thereon.

Dated at Pittsburgh, Pennsylvania, this 14th day of April, 1966.

STEPHEN P. LAFFEY
Referee in Bankruptcy.

Memorandum Opinion, Findings of Fact and Conclusions of Law.

The above named bankrupt, while engaged in the sale of wearing apparel at retail, filed a Petition for an Arrangement under Section 322 of Chapter XI of the Bankruptcy Act on January 10, 1966. The Honorable Joseph P. Willson, U. S. District Judge, permitted the then Debtor to remain in possession, granted additional time for filing schedules to January 31, 1966, the filing of the Plan of Arrangement to February 28, 1966, and referred the proceedings to this Referee.

On February 23, 1966, the Debtor requested the dismissal of its Petition for an Arrangement, requested to be adjudged a bankrupt and asked for the appointment of a Receiver. An Order was entered the same day by the Honorable Joseph P. Willson, appointing Aaron Cohen, Esq., Receiver, and relegating Debtor to bankruptcy.

On February 24, 1966, the Receiver filed a Petition for the sale of all assets located in three stores, or outlets, in New Brighton, Aliquippa and Ambridge, Pennsylvania, alleging same to be of a perishable nature. Sale was fixed for March 16, 1966. Creditors were notified on February 28, 1966, and in the same notice advised of the First Meeting of Creditors to be held on March 21, 1966, at 2:00 o'clock P. M.

At the First Meeting of Creditors and after a thorough examination of one of the officers of said bankrupt, nomination of a trustee was called for. At this time 28 claims had been filed. Harry R. Levy, Esq., representing two of said claims in the sum of $3,714.50, nominated and voted said claims for Aaron Cohen, Esq.,

who had previously acted as Receiver. Attorney Bernard Goodman voted another claim in the sum of $865.55 for Aaron Cohen, Esq., to be trustee.

Attorney Daniel M. Berger, who was acting as local counsel for David Horner from New York, a member of the unofficial creditors' committee formed in New York before a "Plan" was formulated, nominated Norton L. Berman, Esq., a local attorney; also, George A. Hahn, Esq., of the New York Bar, joined in the nomination of Norton L. Berman. At this time Mr. Horner turned over to Attorney Berger 61 claims not yet filed, and George A. Hahn, Esq., turned over his 4 claims for voting. The 65 claims amounted to approximately $113,738.99, a good portion of which included factors.

In the discussion on the nomination Attorney Levy indicated that many of the claims produced by Attorney Berger had been solicited by the creditors' committee and Attorney Goodman made a statement that when he appeared in New York to attempt to effectuate a "Plan" and pay the creditors 35%, or possibly more, he was met with terriffic opposition from Mr. Horner and his group, who demanded a higher percentage which could not be met, and as a result thereof, bankruptcy ensued.

From my experience a liquidation seldom if ever reaches a 35% payment to creditors and it appears that the action taken by Mr. Horner and his group appeared to lack good business judgment and now I find him still trying to direct a proceeding that is virtually liquidated. The only thing that remains to be done is to adjust a fire loss wherein an independent appraisal has been made by a reputable adjustment agency, which has fixed the loss at $11,856.40. This amount can be paid the Trustee immediately and, in my opinion, should be accepted.

To appoint a new Trustee or appoint a committee of creditors would add a financial burden on an estate which in the first place should not have been forced to liquidate.

In view of the foregoing, Aaron Cohen, who had been the receiver, was appointed by me as Trustee on March 21, 1966.

On March 31, 1966, Attorney Berger on behalf of James Talcott Inc., Shapiro Bros. Factors Corp., and Crompton-Richmond Co., Inc., Factors, filed a Petition for Review of my Order Appointing Aaron Cohen Trustee.

There have been turned over to me two letters sent to creditors by the New York Credit Men's Adjustment Bureau, Inc., one dated January 28, 1966, attached hereto and marked Exhibit "A", advising creditors of the Debtor of a meeting to be held on February 3, 1966. The second letter from the same source, dated February 7, 1966, attached hereto and marked Exhibit "B", advised the creditors of the Chapter XI proceeding and that at the meeting of February 3, 1966, 70% of the indebtedness due to trade creditors designated an unofficial creditors' committee and it also advised that it needed the creditors' continued suppport so that it could be elected the official creditors' committee. The last paragraph advised that enclosed was a proof of debt form, followed with "Please note, the power of attorney (referring to the claim) runs to the creditors' committee and/or their representatives and is to be *used solely for the purpose of electing an official creditors' committee and to nominate a tentative trustee. This power shall not be used for the purpose of voting for or against any plan of arrangement, that prerogative being reserved*

for decision of the individual creditor." (Emphasis supplied.)

It is apparent that when the claims were returned to the Unofficial Creditors' Committee they were never intended to be voted on in a bankruptcy proceeding for the election of a Trustee, but only for a "tentative trustee" (Exhibit "A") in a Chapter XI proceeding who may eventually become a permanent Trustee in the event of bankruptcy. The statement is also applicable to the four claims filed by George A. Hahn, Esq., of the New York Bar, said claims being similar to the other 61 claims but for the addition of the names of "Harry A. Margolis or George A. Hahn." See Kal W. Lines, Appellant v. Falstaff Brewing Co., et al., Appellees (9 Cir.), 1956, 233 F. 2d 927, cert. denied, 352 U. S. 893. This case went beyond the present case for there the "Board of Trade" had power to vote the claims. It was pointed out In Re Construction Supply Corporation (E. D. Va.), 221 F. Supp. 124 that "credit corporations seeking to control election of a Trustee may have particular obligations to their members which may in turn conflict with interests of general creditors."

Although this estate has not been fully liquidated, little else remains to be done by the Trustee, Aaron Cohen, Esq., who was the Receiver and who liquidated all the personal property of the bankrupt while acting in that capacity. See In Sloan's Furriers, Inc. v. Bradley, 6 Cir., 146 F. 2d 757, 759. It was for this reason that the election of a creditors' committee was refused in addition to the fact that the motion for same was made on behalf of one of the members of the unofficial creditors' committee which could have learned all things necessary prior to bankruptcy, also the fact that in all probability,

the "committee" would ask for the appointment of counsel, which, in effect, would certainly add to the expenses already incurred in this proceeding. Also, in all likelihood a claim for expenses will be filed by the unofficial creditors' committee, which in the first instance was responsible for this bankruptcy.

FINDINGS OF FACT

1. On February 23, 1966, bankrupt requested that the Court dismiss its petition for an Arrangement, which was filed January 10, 1966, adjudge it a bankrupt, and requested the appointment of a Receiver.
2. On February 23, 1966, bankrupt was adjudicated and the Honorable Joseph P. Willson, U. S. District Judge, appointed Aaron Cohen, Receiver.
3. Due to the perishable nature of bankrupt's goods and merchandise, the Receiver liquidated same by sale on March 16, 1966, which was prior to the First Meeting of Creditors held on March 21, 1966.
4. On March 21, 1966 at the First Meeting of Creditors, two individuals were nominated for Trustee; one was the Receiver, Aaron Cohen, Esq., wherein 3 claims out of 28 claims already filed and allowed in the sum of $4,580.05 were voted in his behalf. The other nominee was Norton L. Berman, Esq., wherein 65 claims not yet filed or allowed in the sum of $113,738.99, solicited by the New York Credit Men's Adjustment Bureau, Inc., were voted in behalf of Norton L. Berman, Esq.

5. The votes accumulated by the New York Credit Men's Adjustment Bureau, Inc., as well as those filed by George A. Hahn, Esq., were based on the Power of Attorney inserted on the claims, which was to be used only for the election of a tentative trustee in the Chapter XI proceeding which failed.

6. Aaron Cohen, Esq., was duly nominated and elected by the claims on file and voted for him, which represented the majority in number and amount of the valid claims filed and allowed, and his bond as Trustee in the sum of $15,000.00 has been filed and approved.

7. This estate is practically liquidated for all intents and purposes, and additional expenses would be incurred by the appointment of a creditors' committee or a new Trustee.

CONCLUSIONS OF LAW.

1. A majority in number and amount of the claims filed and allowed and not having been solicited is sufficient to elect a trustee in bankruptcy.

2. The sweeping supervisory power of a bankruptcy Referee includes a reasoned veto of the selection of a bankruptcy Trustee. Kal W. Lines, Appellant, v. Falstaff Brewing Co., et al., Appellees, (9 Cir.) , 1956, 233 F. 2d 927.

Dated at Pittsburgh, Pennsylvania, this 14th day of April, 1966.

STEPHEN P. LAFFEY,
Referee.

Exhibit "A".

Exhibit "A".

Letterhead of
NEW YORK CREDIT MEN'S ADJUSTMENT BUREAU, INC.

Affiliated With:
New York Credit & Financial Management Assn.
National Association of Credit Management

WAtkins 4-0100

71 West 23rd Street, New York 10, N. Y.

January 28, 1966

TO THE CREDITORS OF:

LENRICK SALES
772 Greenfield Avenue
Pittsburgh, Pennsylvania

Gentlemen:

Please refer to the notices received from Tobin Associates, 180 Madison Aveune, inviting you to the meeting of the creditors of the above company that is scheduled for February 3, 1966 at 1:30 p.m.

This meeting has been *transferred* with the approval of Counsel for the debtor to this office on the same date, the same time in room 1014. Please note the address is 71 West 23rd Street, New York City 10010.

Please make every effort to attend.

Very truly yours,

NEW YORK CREDIT MEN'S
AJUSTMENT BUREAU, INC.
By: GEORGE FELDMAN
George Feldman

GF:jy

Exhibit "A".

Letterhead of

NEW YORK CREDIT MEN'S ADJUSTMENT BUREAU, INC.

Affiliated With:
New York Credit & Financial Management Assn.
National Association of Credit Management

WAtkins 4-0100

71 West 23rd Street, New York, 10, N. Y.

February 7, 1966

TO THE CREDITORS OF:

LENRICK SALES, INC.
772 Greenfield Avenue
Pittsburgh, Pennsylvania

Gentlemen:

On January 10, 1966, the above company filed a petition for arrangement under Chapter XI in the U. S. District Court, Western District of Pennsylvania. The referee handling the matter is Referee Stephen P. Laffey. The petition filed in court listed total assets of $153,314., including $147,500. inventory. Total liabilities were $180,000., including $162,000., accounts payable.

At an informal meeting of the larger creditors representing more than 70% of the indebtedness due to trade creditors, held February 3, 1966, the undersigned were designated to act as an unofficial creditors' committee to represent all unsecured creditors. The attorney for the debtor has been requested by the committee to petition the court to retain certified public accountants to make an audit. Upon completion of the audit, the com-

mittee will report to all unsecured creditors and recommend a course of action which, in its opinion, best serves creditors' interests.

In order that this unofficial creditors' committee may continue to function and be elected the official creditors' committee representing the interest of unsecured creditors, the committee needs your support and cooperation.

Enclosed herewith you will find a proof of debt form. Please note, the power of attorney runs to the creditors' committee and/or their representatives and is to be used solely for the purpose of electing an official creditors' committee and to nominate a tentative trustee. This power shall not be used for the purpose of voting for or against any plan of arrangement, that prerogative being reserved for decision of the individual creditor.

Exhibit "B".

Exhibit "B".

February 7, 1966.

RE: LENRICK SALES, INC.

You are urged to sign the proof of debt, acknowledge it before a Notary Public and affix seal if your company is a corporation. Return it with an itemized statement of account to the Secretary-Agent of the Creditors' Committee, New York Credit Men's Adjustment Bureau, Inc., 71 West 23rd Street, New York, New York, 10010. Please give this matter your prompt attention.

Very truly yours,

CHAIRMAN
Joseph A. Zeller

David Horner
Nathaniel P. McCaffrey
Seymour Benson
Milton Gitenstein

CREDITORS' COMMITTEE
James Talcott, Inc.
Shapiro Bros. Factors Corp.
Crompton Richmond Co., Inc.
London Guarantee & Acc. Co., Ltd.
Riverside Shirt & Underwear Corporation

SECRETARY-AGENT TO CREDITORS' COMMITTEE
New York Credit Men's Adjustment Bureau, Inc.
by Stanley Fuchs/av
Enc.

District Court's Opinion.

MEMORANDUM AND ORDER ON PETITION FOR REVIEW.

WILLSON, *J., District Judge*

Counsel have been heard and the briefs have been considered on the Petition for Review. Referee Stephen P. Laffy has filed his memorandum opinion, findings of fact and conclusions of law as he is required to do under the statute. The Referee has certified that on March 21, 1966, at the first meeting of the creditors, Aaron Cohen was named as Trustee in bankruptcy by him. In the sixth paragraph of the Petition for Review petitioners say that the Referee arbitrarily refused to appoint Norton L. Berman as Trustee — "despite the latter's election by a majority in number and amount of the claims of all creditors present in person or by proxy at such meeting." The Referee has recited in his memorandum the events leading up to and those that occurred during the meeting of the creditors. It appears that at that meeting Daniel M. Berger, Esq., of the Pittsburgh Bar, appeared at the meeting as did George A. Hahn, Esq., of the New York Bar, and nominated Norton L. Berman as Trustee. At this time Mr. Horner turned over to Mr. Berger 61 claims not yet filed, and with Mr. Hahn's claims, a total of 65 claims amounting to $113,738.99 were discussed with the Referee and were to be voted upon for the election of Mr. Berman as Trustee. These proxies were presented to the Referee, and he has found that they were secured as a result of a letter written on the stationery of the New York Credit Men's Adjustment Bureau, Inc., under date of Febru-

ary 7, 1966. The Referee points out that on January 10, 1966, a petition under Chapter XI was filed in this Court and the case referred to Referee Laffey. My order had been entered permitting the debtor to remain in possession, and it was granted until January 31, 1966, to file schedules. The Plan of Arrangement was to be filed on February 28, 1966. On February 23, 1966, at the request of the debtor, the Petition for Arrangement was dismissed, and the corporation was adjudged a bankrupt. On this date, this Court appointed Aaron Cohen, Esq., as Receiver.

It is thus to be noticed that the letter of February 7, 1966, which resulted in the power of attorney from 65 creditors, was written during the time the arrangement was pending. The Referee has found in Paragraph 5 of his findings of fact that the votes accumulated by the New York Credit Men's Adjustment Bureau, Inc., as well as those filed by George A. Hahn, Esq., were based on the powers of attorney secured as a result of the February 7th letter. The Referee further found that this letter related only to the possible Chapter XI proceedings and was directed in the first instance to the creditor's committee, and to nominate a "tentative trustee." The latter phrase is not explained. The point here is that the Referee did not decide that the creditors allegedly represented by the New York Credit Men's Adjustment Bureau, Inc., had no standing as creditors, but simply that the powers of attorney presented by that corporation were insufficient under the circumstances. I agree with the Referee's findings and conclusions in this respect. The letter is clear that any power of attorney should be restricted to the Chapter XI proceedings, and, therefore, I find that the Referee

was correct in all respects in rejecting these claims for voting purposes at the meeting held on March 21, 1966.

The Referee having rejected the proxies of the New York Credit Men's Adjustment Bureau, Inc., and the creditors present not agreeing on the selection of a Trustee, the Referee acted to protect the interests of all creditors by himself appointing the Trustee. The parties before the Referee were in disagreement to say the least. It is to be noticed that the Referee did not accept the vote electing Aaron Cohen as Trustee, but himself named him as Trustee. Under the circumstances he was justified. See Collier on Bankruptcy, § 44.12, page 1662—

> "Accordingly, if the creditors are deadlocked, or for any other reason they may not agree upon the selection of a trustee, the Act protects the interests of all the creditors by requiring the court to appoint the trustee."

It is my view that the Referee had ample authority under the law to adjudicate the issues before him as he did, and, the petition is dismissed, and the Referee confirmed in all respects.

Order

AND NOW, *May 17, 1966,* upon due consideration and for the reasons mentioned in the foregoing memorandum and pursuant to the provisions of General Order 47, the report of Stephen P. Laffey, Referee in Bankruptcy, is in all respects adopted, and the petition for review is dismissed.

/s/ JOSEPH P. WILLSON,
United States District Judge.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 16017

IN THE MATTER OF: LENRICK SALES INC.,
A PENNSYLVANIA CORPORATION,
Bankrupt,

JAMES TALCOTT, INC., SHAPIRO BROS. FACTORS CORP. AND CROMPTON-RICHMOND CO., INC. FACTORS,
Appellants.

APPEAL FROM ORDER OF THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF PENNSYLVANIA

Argued January 20, 1967

Before HASTIE, GANEY and SEITZ, *Circuit Judges.*

Opinion of the Court

(Filed February 15, 1967)

By SEITZ, *Circuit Judge.*

This is an appeal by certain unsecured general creditors ("appellants") from an order of the District Court which dismissed their petition for a review of the order of the Referee in Bankruptcy appointing a Trustee in Bankruptcy of his own choosing.

Appellants are three unsecured general creditors with claims presented at the first meeting of creditors totaling about $44,000.00 out of about $118,000.00 of

such claims. They, along with certain other creditors with claims of about $62,000.00, sought through representatives to vote at the first meeting of creditors for their own nominee as trustee. The right of such representatives to vote was denied by the Referee under circumstances now developed.

On February 23, 1966, after an unsuccessful attempt at an arrangement under Chapter XI, Lenrick Sales Inc. ("bankrupt") was adjudicated a bankrupt and one Aaron Cohen was appointed receiver by the court. The receiver proceeded to liquidate the assets. On March 21, 1966, the first meeting of creditors was held. Unfortunately, no stenographic record was made of the proceedings.[1] The Referee's contemporaneous notes of the meeting are so scanty as to be substantially useless. A predictable controversy ensued as to what there occurred. However, we confine ourselves to the record and the reasonable inferences therefrom.

We do know from the Referee's notes that the bankrupt was examined. We think it fair to infer that representatives of a majority of creditors in both number and amount were present and attempted to vote for their own nominee. However, by an order dated March 21, 1966, the Referee appointed Cohen as Trustee. The printed portion of the caption of the order reading "Order Approving Appointment of Trustee" is stricken. The words "Appointment of Trustee by Referee" re-

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1. Apparently in the Western District parties are free to arrange to have a reporter present at their own expense but the court does not have funds to employ a reporter for the Referee. The Bankruptcy Act provides a procedure for preserving the evidence in such a case, although it was not followed here. See 11 U. S. C. A. § 67(a)(7).

main. Moreover, the order contains a recital that "The Creditors * * * failed to appoint a trustee".

The next development of record occurred on March 31, 1966 when the appellants filed with the Referee their petition for review of the March 21 order. 11 U. S. C. A. § 67(c). It contained numerous challenges to the legality and propriety of the Referee's actions. On April 14, 1966, the Referee filed his "Certificate of Order For Review" with the District Court. It contained a memorandum by the Referee and his findings of fact and conclusions of law ("report"). This was presumably done pursuant to 11 U. S. C. A. § 67(a)(8). Appellants challenge the legality of the filing of findings and conclusions by the Referee after he had the petition for review in hand. In view of our ultimate disposition of this case, we find it unnecessary to decide whether the procedure was here proper. We do recognize that there is a division of authority on this point. But we cannot help but note the obviously undesirable implications of such a practice. Certainly a more appropriate procedure could be adopted as part of the administration of the Bankruptcy Act.

The Referee's findings and conclusions here purport to support the March 21 order of appointment on the ground that Cohen "was duly nominated and elected by the claims on file and voted for him, which represented the majority in number and amount of the valid claims filed and allowed * * *". This finding is diametrically opposed to the ground given in the Referee's own March 21 order.

How did the District Court exaluate the Referee's order and subsequent report? By order dated May 17,

1966, for the reason given in his attached memorandum and pursuant to General Order 47, the District Court "adopted" the Referee's report and dismissed the petition for review, apparently without briefs or argument. In its accompanying memorandum the court said:

> "The Referee having rejected the proxies of the New York Credit Men's Adjustment Bureau, Inc., and the creditors present not agreeing on the selection of a Trustee, the Referee acted to protect the interests of all creditors by himself appointing the Trustee. The parties before the Referee were in disagreement to say the least. It is to be noticed that the Referee did not accept the vote electing Aaron Cohen as Trustee, but himself named him as Trustee."

The quotation shows that the trial court adopted the ground for the March 21 order which appeared in the order itself, i.e., failure of creditors to appoint. In so doing, despite the statement that the report was "in all respects adopted", he necessarily rejected the Referee's finding of fact that Cohen was elected Trustee.

Since fundamentally this appeal attacks the validity of the Referee's March 21 order, we look to see whether it is sustainable on this record on the ground recited in that order and the affirming court order, viz., that the creditors failed to appoint a trustee. In this discussion we shall assume that the Referee's conclusion was based on his finding that a majority of creditors both in number and amount failed to vote.

Although it is not clear that it was raised at the meeting, let us assume that one reason for the Referee's refusal to accept the votes of appellants and others was

that they were based on powers of attorney which, when read with the soliciting letters, did not authorize their holder to use them to vote for the election of the trustee in bankruptcy. We deal with this "finding" because it was the only "rational" basis given by the lower court for its affirmance of the Referee's order. Was such a finding proper and, if so, did it justify the immediate appointment of the trustee by the Referee?

The appellants' petition for review specifically attacked the procedure allegedly employed by the Referee at the creditors' first meeting. Paragraph 8 charged that "The Referee erred in accepting 'innuendos' and hearsay about solicitation as substitution for a hearing thereon with testimony and other proof." The Referee's own report to the court recites that "There have been turned over to me two letters sent to creditors by the New York Credit Men's Adjustment Bureau Inc.". From these letters the Referee and court concluded that the powers of attorney executed by the creditors and presented to the Referee by their representatives were insufficient to show authority to vote. Was the Referee justified in relying on such letters, assuming he had them at the meeting? First, the Referee's notes of the first meeting do not mention such letters. Next, the Referee's report says that such letters were "turned over" to him. Even allowing for informality, this suggests that they were obtained in a non-judicial manner. These factors strongly support the appellants' argument that they were not offered and admitted at the hearing. In such a case it would not be proper for the Referee or the court to rely on them in deciding the matter. Compare In re Augenbaugh, 125 F.2d 887 (3rd Cir., 1942). But even if this material defect was not

decisive, it should have been a red flag to the District Court on review, particularly in view of the clearly erroneous record before him. Some errors have been noticed; another appears in the margin.[2] Certainly the court should not have accepted the letters as though they were decisive of the "authority to vote" issue. Nothing in the "clearly erroneous" review standard prevents a party from being afforded the opportunity to show that a Referee's findings are beyond the pale, particularly where no record was made. At a minimum this matter should either have been set for hearing by the court or referred back to the Referee to have a proper hearing on the disputed issues. There was nothing in the record to indicate a sense of urgency to have the trustee appointed, particularly since the receiver was active.

Nor is the Referee's action justified because he did not allow their claims for voting purposes and the Bankruptcy Act provides that "Creditors shall pass upon matters submitted to them at their meetings by a majority vote in number and amount of claims of all creditors whose claims have been allowed and who are present, except as herein otherwise provided." 11 U. S. C. A. § 92(a). We say this because even assuming, contrary to our belief, that the Referee had a proper record basis for his decision, we think that he was justified in usurping the important right of the creditors to

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2. The Referee's Fourth Finding says that "3 claims out of 28 claims already filed and allowed" were voted for Cohen. The official claim register (Official Form No. 72), showing such claims, has a place to indicate "allowed". Yet it does not note an allowance of any of them even up to the time this record was compiled for this appeal. To say the least, this finding was not supported of record.

appoint the Trustee. Indeed, this right is so important that absent a clear showing of material or prejudicial delay, the hearing to vote on such appointment should, if necessary, have been continued to give the creditors a reasonable opportunity to make their own choice. Compare In re Harris Const. Co., 37 F.2d 951 (D.C.W.D. Pa., 1929)

We think the record does not legally or factually justify the preemptory action of the Referee in appointing the Trustee and thereby depriving the "majority" creditors of a reasonable opportunity to select the Trustee. In fact, such record as we have comes close to compelling the conclusion that the votes in question should have been counted. In any event, we think the record shows that only another meeting of creditors, properly conducted and recorded, can adequately correct the unfortunate series of errors in these proceedings.

All that we have said indicates that the District Court committed error in basing the dismissal of the petition for review on the ground that the creditors failed to appoint a Trustee. Moreover, we cannot condemn too strongly the deviations from acceptable procedural standards which are rampant in this matter. We also deplore the failure of the Referee to keep meaningful summary notes, contemporaneously made, of the important matters arising in proceedings before him when he knew that they were not being recorded. Compare General Order 22.

The trustee-appellee argues that even if we find error we should not reverse. He states that no real purpose is to be served by remanding the matter since the estate is practically ready for distribution. He cites,

for example, Manhattan Shirt Co. v. Tomlinson, 327 F.2d 449 (9th Cir., 1964). There may well be instances where this approach would be justified. However, we think that the circumstances of this case dictate a reversal. We so conclude primarily because anything less would countenance what appears to have been a substantial violation of the creditors' right to appoint a Trustee. Moreover, the appellants and those associated with them before the Referee represented more than 95% in amount of the unsecured claims. Thus, the creditors who were disenfranchised will perhaps be entitled to the great bulk of any distribution to be made. It follows that they will be the ones substantially prejudiced by the delay in distribution and additional expenses which may have to be incurred. Under these circumstances and since the appellants seek a reversal, we think the economic and time factors are not of primary significance. Finally, we desire to emphasize that provincialism and personal preference should have no part to play in the Referee's discharge of his duty to pass on the qualification of the creditors' nominee for Trustee in Bankruptcy.

The judgment of the District Court will be reversed and the matter remanded to the District Court for the entry of an order directing the Referee to vacate the Trustee's appointment and to promptly notice a new meeting of creditors to elect a Trustee.

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.